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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, DECEMBER 18, 2001

APPLICATION OF

CRAIG-BOTETOURT ELECTRIC  
COOPERATIVE

CASE NO. PUE010009

For approval of a functional  
separation plan

FINAL ORDER

On December 29, 2000, Craig-Botetourt Electric Cooperative ("Craig-Botetourt" or the "Cooperative"), filed an application for State Corporation Commission ("Commission") approval of the Cooperative's plan for functional separation ("Plan") as required by the Virginia Electric Utility Restructuring Act ("the Act"), Chapter 23 of Title 56 of the Code of Virginia (§ 56-576 et seq.). The Act requires that the Commission complete its review of proposed plans of separation by January 1, 2002, and that transition to competition be implemented according to a timeline established by the Commission. Pursuant to an Order issued on March 30, 2001, in Case No. PUE000740, the Commission established January 1, 2004, as the deadline for Craig-Botetourt and other electric cooperatives to provide full retail access for their customers.

The Commission promulgated rules<sup>1</sup> for functional separation as required by the Act. These Rules require the Cooperative to file a Plan that includes a cost of service study separating the Virginia jurisdictional operations into functions: generation, transmission, and distribution, subdivided by class and specifically identifying the costs associated with metering and billing. The Rules also require that the Plan include proposed unbundled rates, tariffs, and terms and conditions for service. Requests for waiver from the required submission of documents under the various sections of the Rules are also permitted.

In its application, the Cooperative stated that it is currently functionally separated. It does not own or control any generation or transmission facilities, nor does it own or control any affiliated entity that owns or controls generation or transmission facilities. Instead, Craig-Botetourt purchases all of its requirements for demand, energy, transmission and ancillary services through contracts with Virginia Electric and Power Company, American Electric Power and Southeastern Power Administration. As such, Craig-Botetourt stated that it had no plans to divest itself of any generation assets, to create any new functionally separate entity, or to propose to transfer any functions, services, or employees to a functionally separate

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<sup>1</sup> Commission's Regulations Governing the Functional Separation of Incumbent Electric Utilities under the Virginia Electric Utility Restructuring Act ("Rules"), 20 VAC 5-202-10 et seq., adopted in Case No. PUA000029.

entity or third party. The Cooperative filed a cost of service study, which included proposed unbundled rates to illustrate the Cooperative's rate unbundling. In its application, the Cooperative requested that the Commission waive the requirement of 20 VAC 5-202-40 B 8 of the Rules to file unbundled tariff rates and terms and conditions of service with the Cooperative's functional separation plan. The Cooperative also requested that the waiver extend until the conclusion of this proceeding so it can finalize and submit such filings in compliance with the final order.

In an Order dated March 19, 2001, in this proceeding, the Commission directed the Cooperative to provide notice to the public and established a procedural schedule for the filing of comments or requests for hearing on Craig-Botetourt's application. In that Order, the Commission directed its Staff to investigate the application and file a Report detailing its findings and recommendations on or before July 20, 2001. The Commission also granted Craig-Botetourt's request for a waiver. However, the Commission required the Cooperative to file tariff terms and conditions of service in time for the Commission to consider them and to require notice, if necessary and appropriate, prior to the Cooperative's implementation of retail choice to its customers.

On June 4, 2001, AES NewEnergy, Inc. ("AES") filed a Notice of Protest and request for hearing in this matter.

Specifically, AES requested that a hearing schedule be established to consider issues relating to the allocation of certain costs to the generation and transmission ("G&T") functions, a dual billing option for suppliers, wires charge calculation, and the terms and conditions of service included in any rate tariff or supplier coordination agreement.

On July 20, 2001, Staff filed its Report wherein it recommended that the Commission approve Craig-Botetourt's Plan with the adoption of certain modifications recommended by Staff. Specifically, Staff recommended that the Commission adopt the following: Staff's recommendation to consolidate the Cooperative's G&T functions into one function;<sup>2</sup> Staff's adjustments to the Cooperative's per books cost of service study; Staff's allocations of expense and rate base to the G&T function; Staff's recommendation that the Commission direct the Cooperative to track the costs associated with G&T operations; and Staff's recommendation that the Commission direct Craig-Botetourt to provide tariff rates and terms and conditions of service in time for full consideration by the Commission.

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<sup>2</sup> Staff noted that the Cooperative does not anticipate providing transmission service to customers who shop for energy.

On August 1, 2001, AES withdrew its request for hearing in this case, asserting that it lacked sufficient resources to participate in hearings in every electric cooperative case, and instead intended to focus its resources in Case No. PUE010007, Rappahannock Electric Cooperative's application for approval of functional separation plan.

On August 3, 2001, Craig-Botetourt filed its Response to the Staff Report. In its Response, the Cooperative stated that although it supports Staff's recommendation that the G&T functions be combined, it does not agree with Staff's recommendations pertaining to functional cost assignment. Craig-Botetourt requests that the Commission find that its administrative and general ("A&G") expenses and associated overheads are properly assignable to the distribution function. The Cooperative states that the Commission should recognize that the price paid by Craig-Botetourt to Virginia Electric and Power Company/American Electric Power/Southeastern Power Administration already includes an A&G component and urged the Commission to reject Staff's proposal to assign additional A&G costs to the G&T functions. Further, Craig-Botetourt argued that in its role as the local distribution service provider, it is required by the Act to provide default generation service under its capped rates. According to Craig-Botetourt, supplying default generation services provides a benefit available for all

consumers on Craig-Botetourt's distribution system, including those consumers who may choose an alternative power supplier. Craig-Botetourt further stated that the responsibility bestowed on it to provide default service is a function of its role as the distribution utility. Thus, the Cooperative urges the Commission to reject Staff's proposal to assign A&G costs to the G&T functions.

With regard to the Staff's recommendations concerning uncollectible expense, customer deposits, and interest on customer deposits, Craig-Botetourt agreed that a portion of these expenses should be attributed to G&T, but took issue with the Staff's method of allocation. The Cooperative also noted that the Staff improperly assigned a demand charge of \$4.01 per kW to G&T in addition to the \$.04197 per kWh already assigned for Large Power-Schedule CP-8, and stated that the demand charge should be zero.

On August 27, 2001, the Staff filed a motion for leave to file a Reply to Craig-Botetourt's Response, and its Reply. The Commission granted this motion on October 3, 2001, and permitted the Cooperative to respond to the Staff's Reply by October 25, 2001. In its Reply, the Staff argues that A&G costs should be allocated to G&T, stating that Craig-Botetourt itself incurs certain A&G expenses to support the procurement of wholesale power. Staff also states that if certain A&G costs associated

with wholesale power are shifted to the Distribution function, rates established for Distribution will subsidize those of G&T, contrary to § 56-590 D of the Code, which requires the Commission to set rates that will not result in cost shifting or cross-subsidies between functional units. The Staff also believes that it is appropriate to allocate payroll and related overheads based on an A&G labor factor, and has used a total labor factor to allocate other A&G costs. The Staff responded to Craig-Botetourt's argument regarding the allocation of a portion of uncollectible expense to G&T, stating that because it did not have unbundled revenues with which to make allocations, it used G&T expenses before uncollectible expense as a percent of total operating expenses. The Staff agreed with the Cooperative that it improperly allocated a demand charge of \$4.01 per kW to G&T for Large Power-Schedule CP-8, and agreed that the G&T demand charge should be zero.

On October 25, 2001, Craig-Botetourt filed its Response to the Staff's Reply in which it maintained its position that failure to attribute additional A&G expenses to the generation function does not result in cost-shifting between or cross-subsidization of functionally separate units. The Cooperative argues that payments to its generation and transmission providers already include an A&G component, and therefore the Commission should reject Staff's proposal to shift additional

A&G costs to the G&T function. The Cooperative also reiterated its position regarding the proper ratio for allocation of uncollectible expense, customer deposits, and interest on customer deposits. Craig-Botetourt stated that the unbundled revenues developed in this proceeding should serve as the basis to assign these expenses and deposits in the correct manner.

NOW THE COMMISSION, having considered the Cooperative's application, Staff's Report, the subsequent pleadings, and applicable law, is of the opinion and finds that the application should be approved, subject to the modifications detailed herein.

With respect to the issue of the proper allocation of A&G costs supporting the procurement of wholesale power, we find that the Commission has an obligation pursuant to § 56-590 D of the Code of Virginia to see that no cross-subsidies occur. The function causing the cost should be allocated such costs. A&G costs associated with the procurement of wholesale power support the G&T function, and as such, should not be allocated to the Distribution function. We will, therefore, accept Staff's adjustment allocating certain A&G costs associated with obtaining wholesale power to the Cooperative's G&T function. Further, we accept Staff's functional allocation of labor overheads based on the A&G labor factor.



There are two ways that a cooperative may recover A&G costs associated with the procurement of wholesale power. If a customer remains with the cooperative, the cooperative will recover such costs from the customer. If the customer leaves the cooperative, and the embedded cost of generation exceeds the market, the cooperative will have the opportunity to recover the cost through the wires charge.

We likewise agree with Staff that the allocation factor for uncollectible expense, customer deposits, and interest on customer deposits should be based on each function's relative level of operating expense. We believe this is a reasonable approach in this situation as total G&T expense must be calculated in order to determine the level of G&T revenues, and operating expenses can be used to simulate unbundled revenue.

We find that G&T costs, as defined in this Order, should be tracked prospectively by the Cooperative in order to ensure accurate functional allocations in any future proceedings before the Commission. We also direct the Cooperative to begin tracking the incremental costs associated with billing and collection costs, as well as the activities that give rise to the customer service and legal and regulatory costs.

Craig-Botetourt, through its Wholesale Power Cost Adjustment ("WPCA"), flows through to its consumers changes to fuel charges. Like other cooperatives, these fuel charges

fluctuate monthly. As permitted in § 56-582 B(iv), Craig-Botetourt may also flow changes in its base wholesale power cost charges as they occur, through base rate riders. These riders will also affect the Cooperative's generation costs. It is the Cooperative's position that fuel adjustments can be applied monthly without violating §§ 56-582 and 56-583 of the Code of Virginia, and that changes in purchased wholesale power costs will be passed through monthly under the Cooperative's WPCA clause. We are not persuaded by the Cooperative's argument on this point. However, because it is not necessary that we resolve this issue prior to January 1, 2002, we will defer our consideration of it until next year. In the interim, we direct the Staff to (i) consult with Craig-Botetourt, the other electric cooperatives, and any other interested parties on this issue and (ii) submit a written recommendation to the Commission on or before March 1, 2002, on whether we should implement an annual fuel factor adjustment or WPCA for the cooperatives in lieu of the current fluctuating monthly fuel charge.

Accordingly, IT IS ORDERED THAT:

(1) Craig-Botetourt's Plan for functional separation pursuant to the Virginia Electric Utility Restructuring Act is hereby approved, subject to the modifications discussed herein.

(2) On or before March 1, 2002, the Staff shall submit a written recommendation to the Commission on whether we should

transition to an annual fuel factor adjustment for the cooperatives from the current fluctuating monthly fuel charge, and if so, how such a transition should occur.

(3) Craig-Botetourt shall provide tariffs and terms and conditions of service to the Division of Energy Regulation that conform to this Order and all applicable Commission Rules and Regulations on hundred fifty (150) days prior to its implementation of retail choice.

(4) This case is hereby dismissed, and the papers shall be placed in the file for ended causes.